

## The special drawing right: a formal critic to the dollar dominance in the international monetary system<sup>1</sup>

*Direitos Especiais de Saque: uma crítica institucionalizada à supremacia do dólar no sistema monetário internacional*

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RESUMO: No final dos anos 1960, as discussões internacionais sobre uma possível reforma do sistema monetário internacional originou os Direitos Especiais de Saque (SDR). Embora tenham sido criados inicialmente para representar um ativo adicional para complementar as reservas existentes de dólares e ouro, após a crise do sistema de Bretton Woods o SDR foi considerado um possível substituto do dólar. Baseando-se numa literatura consolidada, o objetivo deste artigo é demonstrar que as origens do SDR não eram exclusivas das negociações financeiras técnicas, mas da convergência de interesses políticos mais elevados contra os Estados Unidos e o domínio do dólar.

PALAVRAS-CHAVE: Direitos Especiais de Saque; ativo de reserva internacional; reforma monetária internacional; hegemonia do dólar.

ABSTRACT: In the late-1960's, international discussions over a possible reform of the international monetary system originated the Special Drawing Right (SDR). While they had been created initially to represent an additional asset to complement the existing reserves of U.S. dollars and gold, after the crisis of the Bretton Woods system the SDR was considered a possible substitute of the U.S. dollar. Relying on a consolidated literature, this article aims at demonstrating that the origins of the SDR were not the exclusive result of technical financial negotiations, but of the convergence of higher political interests against the United States and the dollar dominance.

KEYWORDS: Special Drawing Right; international reserve asset; international monetary reform; dollar hegemony.

JEL Classification: F33; E42; F02.

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## INTRODUCTION

The Special Drawing Right (SDR) consists of an international fiduciary asset created in 1969 by the International Monetary Fund (IMF). Despite maintaining its space, however reduced<sup>2</sup>, in the international monetary order, this monetary instrument was reinvigorated after the outbreak of the 2008 crisis. It had an important role as it provided liquidity to the global economy and supplemented international reserves of the member countries. In 2009 the highest issuing of the SDR since its creation occurred, accounting for a total of US\$ 250 billion. Important proposals to reform the international monetary system after the 2008 crisis, among them the one presented by the United Nations Organization (UN)<sup>3</sup>, emphasized a more active role of the SDR in order to minimize the instability and inequality caused by the dollar dominance in the contemporary international monetary system (OCAMPO, 2012).

As well as in debates on reform proposals in the international monetary system after 2008, the SDR is called upon since its origin to minimize economic and political instability generated around the global structural dependence on the U.S. currency. Therefore, this article aims at arguing how the genesis and the development of the SDR throughout the 1960's and 1970's were surrounded by discussions linked not only to the existing economic problems then, but also to the political discomforts tied to the U.S. dollar dominance and to the privileges resulting from this position of the U.S.A.. For such, initially this study argues about the political-economic context from which the SDR originated, giving emphasis to the criticism by Charles de Gaulle's government to the dollar's central position and to the need for a reform of the international monetary system valid then. Subsequently, it is discussed the functioning of the SDR, such as its rules of allocation, calculation and value. Next, this study enters the debate on the SDR possibilities not only as a complementary asset, but as a monetary instrument capable of replacing the dollar as a key currency in the international economy. The study contemplates as well the reform proposals of the international monetary system, which reintroduced the debates on the SDR after the 2008 crisis, also pointing out some limits of this monetary instrument. Lastly, the final considerations are presented.

## POLITICAL-ECONOMIC PROCESS OF SDR CREATION

The Special Drawing Right (SDR) is an international monetary asset issued by the IMF. It works as a means of reserve and account unit of the Fund and other international organizations. Still under the Bretton Woods agreements, its primary function was to address the existing problems in the monetary system.

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<sup>2</sup> The SDR represented up to 9.5% of international reserves in 1972, however it reduced to 0.5% until 2009 (WILLIAMSON, 2009).

<sup>3</sup> Carried out by Stiglitz (2009), who had as rapporteur Jan Kregel.

The Bretton Woods system was established in 1944 around the monetary standard in which the dollar played the role of international currency. However, the dollar-gold standard would not handle for long the need to increase global liquidity without bringing instability to the global monetary system. Triffin (1960) had called attention to international monetary system's dependence on the U.S. currency, giving special emphasis to the increase in the American deficit due to the U.S.A.'s position as big world liquidity provider. With the dollar demand expansion from the 1960's onwards, due to the global economy increase, dollar issuing surpassed the gold offer. This would necessarily lead to a confidence crisis on the dollar as a reserve asset, as well as on the capacity of the U.S.A. to maintain indefinitely the dollar-gold convertibility – which was known as Triffin dilemma. Therefore, aiming essentially at complementing the use of gold and dollar as global reserve currency, IMF's fiduciary asset emerges.

The SDR was approved in the 23<sup>rd</sup> IMF Annual Meeting in 1968 and the Articles of Agreement alterations, which include SDR, came into force on July 28, 1969. Through this monetary instrument, the goal was to attempt to support trade and finance expansion. Its initial function was to complement dollar and gold reserves, reach a greater payments balance and a more effective process of adjustment in the future (FMI, 2011a). It was expected that countries would manage to increase their reserves without depending on the accumulation of deficits by countries that were big providers of international reserves, chiefly the U.S.A..

As it was not linked to any State, that is, it was not issued by a country but rather a multilateral institution, it would represent a more stable asset when compared to the dollar or any other currency to play the role of international currency. According to the IMF (2013):

The SDR was created by the IMF in 1969 as a supplementary international reserve asset, in the context of the Bretton Woods fixed exchange rate system. A country participating in this system needed official reserves – government or central bank holdings of gold and widely accepted foreign currencies – that could be used to purchase its domestic currency in foreign exchange markets, as required to maintain its exchange rate. But the international supply of two key reserve assets – gold and the U.S. dollar – proved inadequate for supporting the expansion of world trade and financial flows that was taking place. Therefore, the international community decided to create a new international reserve asset under the auspices of the IMF.

Nevertheless, its creation did not occur automatically among countries. It was preceded by intense debating on the international level, which demonstrates the highly politicized dimension IMF's "currency".

Discussions were conducted with divergences, mainly among member countries of the European Economic Community (EEC) and between them and the U.S.A.. France, for instance, was a nation explicitly seeking an international monetary system reform not only in order to bring more stability to the system, but also and, chiefly, to fight the U.S.A.'s privilege of being the main issuer of the international currency.

Until the beginning of the 1960's, EEC countries took measures to support the dollar. However, already in the mid-1960's, they started questioning the fact that the U.S.A. did not respond adequately to their deficits and that the country did not suffer any pressure to adopt measures to eliminate them.

Thus, acknowledging that the American deficit needed to be reduced in order to restore confidence in the system and that gold alone could not satisfy the need for international liquidity in the long-term, most EEC countries started to ponder the emergence of a reserve asset still in 1963. The creation of this new asset could meet the international demand of reserves without any degree of dependence regarding the American deficit or the increasing addition of gold. And, most importantly, if the use of the new asset were linked to gold, all countries, including the U.S.A., would be obliged to manage their external accounts with greater care, which could establish a more symmetrical and less inflationary international economy.

In July, 1965, the then-secretary of Treasury of the U.S.A., Henry H. Fowler, claimed that the country was willing to discuss, on the international level, necessary actions to guarantee substantial improvements in the international monetary arrangements (BORDO, JAMES, 2012). As there was an increment in the use of the dollar as a reserve currency abroad in that time, which increased American obligations internationally, a reform in the monetary order that could guarantee international liquidity to this country was interesting. If promoted, this reform would make possible to reduce pressure on the dollar and avoid an U.S. currency crisis.

This period was marked by convergences and divergences among countries regarding the wish to increase or reduce the dollar use as main international reserve currency. The possibility of more intense American control over the payment balance was also in the agenda.

In particular, EEC countries began to worry about the role of the U.S.A. and the dollar in the Bretton Woods system due to: i) the return of economic growth which basically resulted in the formation of the Common Market in 1958 and it included big surpluses in payment balance and increase in international reserves; ii) gold scarcity from the 1960's onwards, which brought, for the first time since the post-war period, fear that the U.S.A. would not be able to guarantee dollar-gold convertibility at 35 dollars the ounce; iii) the high increase of the American deficit starting in 1958, with an annual growth of US\$ 1.5 billion to US\$ 3.5 billion; iv) the instability, already pointed out by Triffin (1960), caused by insufficient American gold reserve, which would incapacitate the country to exchange all the existing dollars in foreigners' hands; v) the growing conviction that the American deficit was causing inflation both internally and externally; vi) the idea defended by France but somehow shared by the other countries that American deficits gave the U.S.A. the possibility to control European economies; vii) the frustration with the existing asymmetries in the Bretton Woods system that allowed the U.S.A. to incur payment balance deficits; viii) the perception that the European countries could do little to change the growing American deficit and that in fact they were obliged to accept any dollar from abroad in order to avoid the appreciation of their currencies against the U.S. currency (SOBOL, 1982).

EEC was convinced that it had already helped the U.S.A. enough and that the time had come for the Americans to take more responsibility in the control of their

payment balance. Europeans defended that despite the American deficit reduction going contrary to the greater need of international liquidity, on the other hand, it would help to restore confidence in the dollar as a reserve currency, decreasing inflationary pressure and bringing more stability to the existing monetary order.

In that moment, however, there was still no consensus among Europeans on the reform, despite a generalized dissatisfaction. For instance, the Netherlands defended a dollar participation decrease in international reserves. Germany and Italy, in turn, did not want to commit to limiting the dollar participation in their reserves in the future once they were afraid to wear out the good political relation with the U.S.A.

Nevertheless, the great majority of the EEC components believed that it would be necessary to create a new reserve asset as a means of reducing the dependence on the dollar and on the big American payment balance deficits: “[...]by creating a new asset, they would help eliminate or at least reduce the use of the dollar as a reserve and at the same time restore gold to a more central function in the Bretton Woods system [...]” (SOBOL, 1982, p. 361).

### **The debate on monetary system reform in France**

With French president Charles de Gaulle in the debates on the international monetary system reform proposal, monetary issues, so far mostly restricted to central bank experts and technicians, gained denser political outlines. Discussions among countries on the role of the dollar and gold in the international economy would become ever more disputed.

The French were, on the international monetary policy level, the ones who most directly challenged the U.S.A. and the dollar in the 1960's. While the other EEC countries sought to shield themselves through technical jargon on the possible dissatisfaction regarding the dollar, France did not hide its discontentment. France blatantly showed its unhappiness to what it viewed as a privilege to the dollar position in the Bretton Woods system and the possibility of the U.S.A. maintaining persistent payment balance deficits.

The French argued that the Bretton Woods system had become unfair due to the privilege that countries that issued reserve currencies possessed and the U.S.A. in particular. There was an inherent weakness in this regime, which concerned the possibility of reserve currency issuers to pay their deficits in their own national currency. That gave more action liberty to these countries with regard to those that needed to pay their deficits in currencies that they could not simply create, but only obtain through surpluses in the payment balance of loans. With this freedom, the issuers could increase their external expenses without regarding their revenues until they reached a point, occasionally, in which they could suspend the convertibility of their currencies: “In the United Kingdom's case, from pounds to dollars and, in the U.S.A.'s case, from dollars to gold” (Idem, p. 309).

Therefore, France sought to substitute a monetary system based on the dollar for another more directly linked to gold. Thus, France envisioned the possibility of leaving the U.S.A.'s dominance zone, being exempt from the obligation of accumulating dollars in its reserves with the objective of avoiding French currency appreciation compared to the U.S. currency. By depending exclusively on gold, France

believed that this fact could eliminate inequalities that had become structural. Finance minister at the time, Valéry Giscard d'Estaing, claimed in the IMF and World Bank national meetings in 1964 that:

The world monetary system must be set in concentric circles: the first one being gold, and then, the second, if necessary, recourse to deliberate and concerted creation of either reserve assets or credit facilities. The inner circle is gold. Experience in recent years has shown us that, aside from any theoretical preference, gold remains the essential basis of the world payments system (DE VRIES, 1976, I, p. 40, apud BORDO, JAMES, 2012, p. 118).

It is worth stressing that until 1962, France had refused to have a more direct position against the dollar's centrality. France did not wish to challenge directly the U.S.A. and the dollar so that it would not jeopardize the system's stability as a whole. At that time, France was worried about rebuilding its own economy and finances, which were deteriorated.

The change regarding the initial stance was the result of some factors. Firstly, France's stabilization plan instituted in 1958 and the franc depreciation by 17.5% in December of that year. With these measures, the country reached record surpluses in its payment balance (US\$ 1.2 billion in 1961 and 1962) and also increased its international reserves, which grew 46% between 1960 and 1961 (SOBOL, 1982). Secondly, the Common Market was consolidating and the French could compete effectively with other countries, thanks, in particular, to their currency's substantial depreciation. In third place, in 1962, with the end of the war in Algeria, which had consumed political energy and economic resources, France was in the process of developing its own nuclear attack force: "a new climate of relative domestic stability and economic prosperity provided a safe base from which they [French] could attempt to restructure the international monetary system so that it would increase the independence of their own country [...]" (Idem, p. 313).

France proposed in 1963 the creation of the European Currency Unit, which would be linked to gold and would be composed in proportions fixed by the currencies of the ten largest economies then. Therefore, the French believed that they would be able to increase gold value and, so, restore the international monetary order based on the metal. Its main objective was to facilitate providing additional credits, with a strict institutional control. This way, the French proposal would give more power to the IMF. Due to French demands, in July 1967, the word "reserve" got away from discussions regarding the ECU and the concept was restructured and began to be called "Special Drawing Right" (SDR) (BORDO, JAMES, 2012).

Many of the other EEC nations converged with the French desire to establish greater symmetry in international monetary relations and to exert some control over the enormous amount of dollars that they were obliged to accumulate in their reserves. This convergence of interests, added to their wish to maintain EEC unity made them sympathetic to France's obsession. What mattered to the others was not necessarily the anti-American policies that the French followed at that moment (SOBOL, 1982).

However, as already shown, there was no consensus in the EEC regarding the French positioning before the U.S.A.. Germany and Italy, chiefly, sought to keep a

good relation with the U.S.A. during the 1960's in order to guarantee the American commitment with Europe's defense in the Cold War context. They also feared that a direct attack to the dollar could unbalance the international monetary system.

Despite Europeans' different positions, the preoccupation with international liquidity remained throughout the 1960's. Consequently, EEC's interest that the U.S.A. should reduce their deficits was maintained.

As opposed to the French, who wanted to strengthen the gold standard and the end of the dollar as a reserve currency, many of the EEC countries were willing to conceive the dollar as an international reserve currency. The most indirect tactic of accepting that part of the liquidation should be done in gold could allow them to not enter the confrontation with the Americans. The U.S.A., by wishing a new form of creating liquidity, did not want the new asset to have any relation to gold, because then there would be no pressure on their metal reserves, which would not put the system's stability at risk. This way, the Americans and many of the EEC countries insisted that the new asset should work as additional reserves in order to reduce the pressure regarding the dollar and gold. France, isolated, ended up giving in and nothing was done to limit the U.S.A.'s ability to continue incurring payment balance deficits.

Although the French version was defeated, the reform was not put aside. It became evermore urgent given the decrease in gold reserves. (BORDO, JAMES, 2012). Facing this, the EEC countries agreed that the SDR could represent a useful and necessary improvement in the way that international reserves were traditionally created, even though they recognized that the new asset would not impose any disciplinary action on the U.S.A. concerning its deficits control. In any event, the SDR could represent a bigger space for Europeans in the global community once it would make possible the creation of liquidity to be more linked to the needs of international economy than to the U.S.A.'s payment balance deficits.

## HOW SDR WORKED

One sophistication mark of this new monetary instrument is the fact that the IMF, as the SDR issuing institution, did not have to use its own resources for the establishment of this new asset, not even for its utilization by the member countries of the Fund. In the SDR allocation process, participants would receive an increase in their reserve assets without reducing that of other countries'. This way, there would no longer be the need to deplete a country's reserves offer when another country wished to increase theirs.

The SDR soon received a nickname, despite pretentious and inaccurate: "paper gold". IMF's own accounts were denominated in SDR and several other international organizations also adopted it as an account unit.

The intensively politicized debate that preceded the creation of the SDR ensured that the new instrument was surrounded by regulations. It would be managed in a separate account in the Fund. Already existing activities would be conducted by the General Account. Operations and transactions involving the SDR would, in turn, be conducted by the Special Drawing Account. Moreover, the SDR could only (and this has been kept until current days) be used in transactions involving

the IMF and its members. They had the right but were not requested to join the scheme. Participation was allowed for IMF members, non-members and institutions that played the role of central banks for more than one member country (FMI, 2011a). In this last category are framed regional organizations in which their members and central banks gather part of their reserves.

All decisions concerning the allocation and cancellation of the SDR needed to have at least 85% of the votes from member countries, as well as any change regarding this percentage. SDR allocation to each country would be proportional to the quota of each one inside the Fund.

It was agreed initially that the countries would use the SDR only to meet the payment balance needs, complementing existing reserve assets, and not to change the composition of their international reserves. With the prohibition, the acquisition of dollars to convert to gold by using this asset could be avoided.

Until May 1972, the SDR value was linked to gold and had an interest rate of 1.5%, below the existing interest rates at the time, which discouraged its use as a reserve. The SDR value corresponded to 0.888671 grams of gold, exactly as the dollar during the Bretton Woods system (Idem). With the generalized fluctuation of currencies, after 1973, the SDR began to be calculated based on a basket of 16 currencies, selected according to the percentage (at least 1%) that they had in the international trade of goods and services between 1968 and 1972.

While the 16 currencies were references to determine the SDR value, only five were used to define its interest rate. And this dichotomy between the determination of the interest rate and the SDR value started to become an obstacle to its price establishment inasmuch as the IMF sought to increase the acceptance of its asset in the financial markets. Therefore, the Executive Board considered the possibility of unifying the two baskets (one that determined the interest rate and the other that determined the SDR value) and reducing the currency basket to five currencies. Thus, the new IMF director at the time, Jacques de Larosière, proposed to evaluate the new identical basket to the one already used to determine the SDR interest rates.

Since 1981, the currency basket became composed of only currencies from the five most industrialized countries (G5) – dollar, yen, Deutsche mark, pound and the French franc – in order to guarantee that the SDR would be stable before the oscillations in exchange rates. Subsequently, the euro would replace the mark and the franc. However, the weight of every currency depended on its value at the time. In January 1981, when the new basket was already operational, changes in the interest rate, along with the dollar appreciation, made the weight of the U.S. currency rise from 31% (old currency basket) to 43%. And, since the dollar kept its appreciation during the first half of the 1980's, it rose from 43% to 56% in February 1985 (BORDO, JAMES, 2012). Afterwards, it fell. With a new system that came into force, which revises the weight of each currency in the basket every five years, the dollar participation decreased. After the first revision, the U.S. currency started to compose 42% of the basket.

IMF's Executive Board performed its last assessment of currency weight, which determines the SDR value, after 2011 – a proportion that will keep for the next five years. The weight of every currency from 2011 to 2015 corresponds to: U.S. dollar (41.9%); euro (37.4%); yen (9.4%); pound (11.3%) (FMI, 2011b). Despite all ef-

forts for greater balance among different currencies, the dollar still keeps its preponderance. In 2016 a new revision of the currency baskets that compose the SDR value will be accomplished, and China is articulating with the IMF the possibility of including its currency, increasing the importance of the renminbi internationally (BEATTIE, 2015).

## THE SDR AFTER BRETTON WOODS: A VIABLE ALTERNATIVE FOR THE DOLLAR?

The original objective of the SDR was to complement the U.S. currency as a reserve asset. However, with the end of dollar-gold convertibility in 1971, the increase of dollar offer was made possible. This way, in this first moment, there was no more need for the existence of an asset that worked as supplementation to the U.S. currency. However, a few years afterwards the SDR was given the possibility of acquiring a new meaning in the international monetary system. It became a possible substitute for a determined portion of dollars that central banks had in their portfolios. It would be admissible, thus, to diversify the reserves beyond the U.S. dollar (BOUGHTON, 2001).

With the persistent depreciation of the dollar in the beginning of the 1970's, both the IMF and central banks analysts started to seek alternatives to an international reserves system based on the dollar. With the end of dollar-gold convertibility, it was estimated that 70% of all official reserves that were not gold would be in dollars. A solution would be to diversify the reserves to other tradable currencies. At the time, there were two main alternatives: the Deutsche mark and the yen. However, Germany and Japan were reluctant in internationalizing their currencies and having them used as a reserve. Similarly, a multiple reserve currency system was seemed as potentially unstable. Then, the SDR returns as a viable alternative.

The IMF began this effort around the SDR through the creation of a Substitution Account. There were two attempts for its implementation: the first one in 1974 and the second after 1978. It basically had two objectives: first, to strengthen stability in the exchange market by providing foreign central banks with the means to reduce their dollar reserves that did not involve selling the U.S. currency in private markets; secondly, to help transform the SDR in the main reserve asset in the international monetary system (GOWA, 1984, p. 664).

Nevertheless, there were limits that needed to be overcome for the SDR (through the Substitution Account) to become an important international reserve currency, namely: i) the fact that they were still a newly created asset with very little known properties; ii) the SDR stock was small in comparison with that of the dollar; iii) although the SDR could be exchanged among central banks and other official agencies, there was no private market for the SDR; iv) it was a financially attractive asset, mainly due to the fact that it had a much lower interest rate than those of other assets.

Therefore, the final report of the Committee of Twenty (*ad hoc* committee for the international monetary reform and related topics) foresaw the possibility of creating a Substitution Account, given the divergences and obstacles, a specific

proposal was not endorsed. After some years forgotten, the idea of creating a Substitution Account resurfaces amid a strong process of dollar depreciation. In 1978, an effort restarted to reform the international monetary system through the Substitution Account establishment. It was conducted by the IMF staff and representatives of the Fund's member countries, and it had the support, in particular, of the U.S. Treasury. As in the previous proposal, the aim of the Substitution Account was to deposit dollars and in exchange to issue certificates denominated SDR (GOWA, 1984). According to Boughton (2001), two differences regarding the first proposal to create a Substitution Account become evident: 1) the revised proposal should be voluntary so that it had some chance of being approved; 2) the U.S.A. should be excluded or discouraged of participating in the Substitution Account. Only this way could the inherent asymmetry between the U.S.A. and the other countries be reduced: "If any country could deposit dollars in exchange for SDRs, then the United States alone could finance a deficit by issuing its own currency and bypassing the foreign ex-change market" (BOUGHTON, 2001, p. 938).

In 1979, at the moment the dollar was falling progressively in the exchange market, there was a real confidence crisis in the U.S. currency. At the crisis climax, IMF director and head-economist of the Fund, Jacques J. Polak, began to develop a more thorough plan about the Substitution Account, in which the IMF would establish and manage it and central banks could voluntarily deposit dollars and in exchange receive the SDR credits. It could be used in a limited way according to the established rules.

To Boughton (2001), this was a good moment to create a Substitution Account, both for the most immediate need to combat the dollar depreciation in the exchange market and for the wish to transform the SDR in the main reserve asset in the international monetary system, as demonstrated Article VIII, section 7, of the Article of Agreement:

Each member undertakes to collaborate with the Fund and with other members in order to ensure that the policies of the member with respect to reserve assets shall be consistent with the objectives of promoting better international surveillance of international liquidity and making the special drawing right the principal reserve asset in the international monetary system. (FMI, 2011a, p. 26).

The U.S.A. seemed to have interest in stabilizing the demand of its currency and also end the excessive dollar participation without depreciating its value. For that, it could be expected from the Americans that they would pay part of the costs to change to a more stable monetary system, both through the payment of higher interest rates which were previously paid in reserve assets, and by taking a contingent liability for covering the exchange risk. However, it was not unanimous in the country, considering, in particular, the U.S. Treasury staff.

The support to the proposal of Polak and Lavosière culminated in the endorsement by part of the IMF Interim Committee in October 1979. The Substitution Account establishment was the main item in the Committee's agenda at the meeting in Belgrade. In it, it was claimed that the Substitution Account "if properly designed

could contribute to an improvement of the international monetary system and could constitute a step toward making the SDR the principal reserve asset in the system” (IMF *survey*, 15 october, 1979, p. 315, apud GOWA, 1984, p. 667). It seemed like the ideal moment for the SDR to become the main international reserve asset.

Nevertheless, negotiations ended in a big stalemate in April 1980. Therefore, the meeting in Belgrade in 1979 was the climax of the Substitution Account’s short life. There was no consensus among American authorities on the advantage of increasing the role of the SDR as a means of limiting a speculative pressure against the dollar. The biggest enthusiasts of the project were the European countries that sought to diversify their reserves, even though the degree of support to the movement was varied. This proposal became politically unacceptable especially due to the questionings about who would bear the costs of implementing the Substitution Account. It could, under certain circumstances, incur financial losses. The Account would pay interest on certificates denominated in SDR but it would receive interest on dollars invested in U.S. bonds: the balance between paid interests and received interests could be negative. Loss could also occur if the dollar depreciated with regard to the currencies that compose the SDR.

Most American authorities rejected the idea of converting short-term liabilities for central banks to long-term liabilities for the IMF. Since long-term interest rates were usually higher than those of short-term, the conversion could end up expensive to the U.S.A. This way, the American Treasury reckoned that the establishment cost of a Substitution Account would be heavier than the benefits of a more stable monetary system.

In order to try and minimize these costs, the U.S.A. sought adhesion to what came to be known as the Gold-only solution. In this proposal, only IMF’s gold could be used to support possible deficits of the Substitution Account. In case this action was insufficient, the American Congress could be questioned if it could claim a part of the remaining deficit.

This proposal would practically impose no cost to the U.S.A. and, because of that, the other G5 members did not accept it. Although IMF’s gold committed with the Substitution Account was sufficient to cover potential losses, Europeans and the Japanese opposed to this resolution at first as it would not involve any financial commitment by the U.S.A., except in an extreme scenario (GOWA, 1984).

Other G5 members sought together an international monetary system reform that could reduce the American privileges and, because of that, they focused explicitly on the distribution of potential financial costs to the Substitution Account. With part of these costs directly accrued to the U.S.A., the Americans would have to reduce their expenses abroad restricting, thus, their privilege of freely incurring deficits in the payment balance. Therefore, Europeans and the Japanese combated the Gold-only solution as it would need, in part, Americans to hold their position in the international monetary system and restore the extraordinary ability they had during the Bretton Woods period. However, the U.S.A. did not sacrifice its political autonomy for the Substitution Account.

There was a direct relation between the dollar oscillations and the increasing and decreasing interest over the Substitution Account. The dollar depreciated sharply in 1977 and 1978, fluctuated in 1979 and began to appreciate rapidly in the early-1980’s

after Paul Volcker's shares at the head of the Federal Reserve (Fed). Following the same direction, discussions over the Substitution Account gained space when the dollar was depreciating or fluctuating (1974, p. 1978-1979) and were quickly ceased at the moment the dollar became stronger at the beginning of the 1980's.

The dollar depreciation raised interest in the Substitution Account due to the fact that it could make possible the diversification of reserves beyond the dollar without creating disarray in the exchange market. Nevertheless, the dollar appreciation in the early-1980's discouraged its sale and, thus, eliminated the needs to create a Substitution Account (Idem).

Consequently, with the unilateral decision of breaking the dollar-gold convertibility in 1971, along with the dollar appreciation through Volcker's policy in 1979 (raising the American interest taxes to two digits), the U.S.A. managed to reestablish confidence in the U.S. currency and the international economy. Therefore, the probability of creating the Substitution Account was undermined and, consequently, so was the possibility that the SDR could supplant the U.S. currency as a global key currency. There is, thus, a clear relation between interest in implementing the Substitution Account and the destination of the dollar in the international monetary system.

Once more the SDR lost the chance of consolidating itself as an important monetary instrument in the international economy by failing to implement the Substitution Account. However, in some aspects the IMF asset gained importance and more acceptability from the 1980's onwards.

Boughton (2001) argues that the dollar instability throughout the 1980's strengthened the SDR quality as a more stable alternative than any other currency of influence in the international economy. Not only due to the decrease in the number of currencies in the basket that compose the SDR, but also to their increased volatility, each internationally important currency fluctuated abruptly in relation to the SDR in the 1980's.

The running total of the SDR in the payroll of the IMF SDR Department increased 130% between 1979 and 1989. The initial SDR stock (allocated between 1970 and 1972) totaled 9.3 billion SDR. Between 1979 and 1981, there was a second round of allocations, totaling 12.1 billion SDR (Idem). And there would be no more allocations of SDR until the 2008 crisis when, to help mitigate the financial crisis effects, a US\$ 250-billion allocation of SDR was made on August 28, 2009, the largest of its history. In September of that year, a new SDR issuing was done, totaling US\$33 billion (FMI, 2009).

The IMF attempted during the 1980's to increase the SDR liquidity and acceptability. Some measures were effective, such as allowing central banks to use the SDR routinely without having to justify or reverse the transaction afterwards. Many countries started to use the SDR in a more stable way and, thus, the Fund tried to make its asset more competitive. During its creation, it was originally thought to be used in immediate transaction liquidations among the countries or between the countries and the Fund. In the late-1970's, though, this policy began to clash with the wider objective of transforming the SDR into a financial asset. Therefore, the IMF started to allow member countries and others to use the SDR in swaps, long-term transactions, loans and donations. However, this attempted SDR liberalization

had a limited effectiveness since the demand of this monetary instrument was just slightly expanded (BOUGHTON, 2001).

Another attempt by the IMF in order to expand the market for its asset was the creation of a network of SDR “keeping holders” among regional development banks and central banks. The Bank for International Settlements (BIS) was nominated a keeping holder in 1974 and it worked as a short-term currency supplier for central banks, making temporary exchanges of currencies for the SDR. Only the BIS, the IMF and other participating countries could maintain or deal the SDR. In the 1980’s, the IMF expanded to 16 the number of keeping holders. However, the stock of these institutions was insignificant, less than 0.1% of the total SDR until the end of the 1980’s (Idem).

In addition to the fact that the dollar had stabilized its value, the capital markets development also limited the attractiveness of the SDR, in which central banks and other agents could diversify their risks beyond the SDR. For example, the ECU, predecessor of the euro, was a more attractive alternative to the SDR once it had a more expanded market and was subject to fewer restrictions. Another reason for the low demand of the SDR was the lack of an official pricing system of this asset for the market.

Another SDR limiting factor refers to the fact that its interest rate was not directly related to market evaluations, in addition to being subject to complex rules, which discouraged the growth of a deeper and more liquid market. It would be necessary a more flexible SDR official pricing and the maintenance of a more open market.

With the higher dollar stability in the early-1980’s, the countries worried less and less with their possibilities in diversifying their portfolios into other currencies. At the same time, these States would become more distressed regarding the poor SDR trading. Consequently, they gradually lost their interest in linking their currencies to the SDR. Midway through this century, there was a peak concerning the linkage of other currencies to the SDR, which occurred when the dollar was depreciated (after 1985 with the Plaza Agreement). A few years later, many of these countries decided to adopt other agreements and a minority linked their currencies to the SDR. Only seven countries officially linked their currencies to the SDR until the end of 1989 and this number fell even further at the beginning of the 1990’s (Idem).

### **The SDR in the 2008 crisis and its limitations**

As discussed above, after nearly 30 years there was a record SDR allocation in order to combat the international 2008 crisis effects, totaling US\$250 billion. A major part of the reform proposals that surfaced at that moment revived the debate on the advantages of this monetary instrument for the global economy.

A document elaborated by the chairman of Chinese central bank released in 2009 was the trigger that made the SDR return to the debate on the international monetary system reform. It reported the importance of the existence of a stable international reserve currency, issued according to clear and well-defined rules, in addition to its flexible offer in order to adjust to demand changes (ZHOU XIAOCHUAN, 2009). In this sense, the SDR use should be increased and also adopted by the private sector, such as for the payment of trade and financial trans-

actions, for instance. The Chinese document does not directly mention the dollar, but by defending a more stable key currency, it clearly attacks its centrality and the instability caused by a national currency that plays the main role as an international currency. Among the problems are the privileges that this condition offers the Americans and that contribute to expanding chronic deficits in their accounts. Moreover, with the crisis, at least at a first moment, the dollar centrality and the U.S. debt bonds have been called into question. In this context, not only China but also the BRICS, G-20, besides studies carried out by Stiglitz (2009), Ocampo (2012), among others, reasserted the advantages of the SDR for the international financial and monetary system.

However, despite its revival in the reform proposals and in its record allocation in 2009, the SDR position in the international economy is still not that relevant. Some of the problems that still limit the demand of this monetary instrument are related to the fact that governments can use it only for payments with the IMF, without the possibility of utilization in the exchange market or in other market transactions. It would be necessary to develop private markets in which the SDR could be bought and sold and the creation of liquid markets in which governments and corporations could issue bonds in SDR at competitive prices. The first SDR bond issuers would have extra costs due to the novelty of the instrument, that is, the SDR would present low liquidity. In this way, they would have a competitive disadvantage because of the existence of liquid asset markets denominated in dollars and in euros. To ensure a more relevant role of the SDR as a reserve currency, it would be necessary for governments to invest for a long period (EICHENGREEN, 2009).

Another limiting challenge refers to the non-existence of an exchange market based on the SDR. The possibility of trading the SDR with private and official participants would be necessary. The IMF also does not have the capacity to issue additional SDR quickly in shortage periods to ensure liquidity. In addition, due to its lack of free acceptance in private markets, central banks would need to enable the Fund's voluntary agreements and wait from five to ten business days to have their SDR participations traded by free course currencies. However, it is necessary to act rapidly when an intervention in the exchange market is called upon and waiting days for such operation can further deepen a crisis (Idem).

The member countries' vote power is directly related to the quota each possesses inside the Fund. Quota calculations correspond to a weighted average of the GDP (weight of 50%), openness (30%), economic variability (15%) and international reserves (5%) (FMI, 2016). The U.S.A. is the only country that holds the biggest number of votes. Many of the Fund's decisions, including the increase of the quota number for each member, depends on the approval of at least 85% of the countries, a big disadvantage for the U.S.A. that solely has a quota of 17.4% – considering the quotas reform ended in 2015 (FMI, 2011c). That way, any attempt to increase the importance of the SDR in the international economy or even to think of it as an alternative to the dollar as an international reserve currency will depend on the U.S.A., since this country is predominant inside the very IMF. That is, it would ultimately be the Americans decision to increase the weight of the SDR as opposed to their own currency. Now it is fit to question if the Americans would be willing to give up being the largest key currency issuer of the international monetary system.

## FINAL CONSIDERATIONS

This study aimed at presenting the debates that permeated the rise and the development of the SDR during and after the Bretton Woods system. IMF's "currency" was always thought as a monetary instrument capable of minimizing distortions caused by the predominant role of the U.S.A. and the dollar in the international monetary system. Beyond eminently economic issues related to the problems of a monetary order based on the dollar, discussion on the SDR had a strong political bias, due to the discomfort before the American privileges caused by the dominance of their currency.

In the context of this structural dependence of the Bretton Woods system on the dollar and on gold, from 1963 onwards the European countries, largely, started to ponder the creation of an asset to complement international reserves of the U.S. currency and gold, meeting the demand of reserves with no connection with the growing American deficit. As demonstrated, however, this debate was surrounded by divergences both among EEC countries and between them and the U.S.A. De Gaulle's France openly questioned the role of the U.S.A. and the dollar in the established order and sought to restore a system more directly linked to gold thus breaking with the dollar restraints. Countries such as Germany, in turn, wished for a monetary reform, however, without having a direct confrontation with the U.S.A.

In 1969, the SDR came into force, but a short time afterwards the Bretton Woods system collapsed and the need for a complementary demand of dollars and gold lost its meaning. However, given the dollar depreciation and the monetary instability established, the SDR had a new meaning before the creation of a Substitution Account. Between 1978 and 1979, there was the expectation that the SDR would not only complement but also substitute part of the international dollar reserves. There was a probability, thus, of diversifying reserves beyond the U.S. currency. Nevertheless, after Volcker's policy in 1979, resulting in the appreciation of the U.S. currency, the expectations of diversifying reserves beyond the dollar were undermined. Therefore, it can be seen how the SDR history in the international order was intertwined with the dollar movements and how they were thought for specific economic conditions that did not become a reality.

Thus, the highly politicized debates on the SDR and on the dominant position of the dollar in the international monetary system demonstrate how the currency is more than just an issue restricted to technocrats from central banks, but it also has a political and social aspect. It is the expression of the economic, political and military power of its issuing country/institution. This study hopes that there will be an increase in future reflections also in the post-2008 crisis monetary order, in which the SDR appear once more as a possible alternative, while its remnant limitations, before the instabilities caused by the dependence on the monetary regime of the U.S.A. and their currency.

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